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## Cabinet Approves Supplementary Budget

On June 23 the Japanese cabinet approved a Y2.08 trillion ($14.9 billion at Y140=$1.00) supplementary budget for FY 1987 (April 1, 1987-March 31, 1988) that will be submitted to a special session of the Diet in July. The extra expenditures, the largest in 13 years, are necessary to implement the Y6 trillion ($42.9 billion) stimulus package adopted last month. Local governments and the business sector are expected to provide Y3 trillion or so of the Y5 trillion ($35.7 billion) increase in spending called for in the package. In addition, the tax reform legislation that will be submitted next month (see JEI Report No. 24B, June 26, 1987) is expected to result in a tax cut of about Y1 trillion ($7.1 billion).

The additional spending will be funded in part by Y1.36 trillion ($9.7 billion) worth of government construction bonds (see Table 1). Other revenue sources include the budget surplus carried over from FY 1986 and funds from the sale of some of the Nippon Telegraph and Telephone Corp. stock Tokyo holds.

The government expects to earn Y5.5 trillion ($39.3 billion) from the sale in FY 1987 and will use the bulk of the money to redeem outstanding government bonds.

Table 1: FY 1987 Supplementary Budget*

(in billions of yen)

| Expenditures | Amount |
|---|---|
| Public works | Y1,358.5 |
| General public works | 800.0 |
| Disaster relief projects | 343.5 |
| Infrastructure | 215.0 |
| Non-interest bearing loans | 458.0 |
| Small- and medium-scale business programs | 41.4 |
| Government procurement | 101.1 |
| Economic cooperation | 18.3 |
| Subsidies for public housing | 179.0 |
| Interest payment from the increase in the national debt | 50.5 |
| Other | 0.8 |
| Reduction in interest payments | -128.3 |
| Total | 2,079.3 |
| **Revenue** | |
| Construction bonds | 1,360.0 |
| Surplus carried over from FY 1986 | 403.0 |
| Revenue from sale of NTT shares | 458.0 |
| Local governments' contribution to public works | 25.3 |
| Funds for the Bank of Japan | -167.0 |
| Total | 2,079.3 |

*Change from the initial general account budget passed in April 1987.

Source: Nihon Keizai Shimbun, June 24, 1987.

The plan to stimulate domestic demand marks at least a temporary end to the fiscal reconstruction program that had reduced government bond issues in each of the past four fiscal years (see Table 2). The supplementary budget raises general account expenditures to Y56.18 trillion ($401.3 billion), up 4.4 percent from the revised fiscal 1986 figure (see JEI Report No. 1B, January 9, 1987). Bond issues will rise to Y11.86 trillion ($84.7 billion), although they will underwrite the smallest proportion of government revenue -- 21.1 percent -- since FY 1975. In addition, the cabinet decided last week to add Y845.2 billion ($6 billion) to the Fiscal Investment and Loan Program, the so-called second budget that is financed primarily by postal savings and public pension funds, raising total FILP expenditures to Y27.93 trillion ($199.5 billion), a 16 percent hike.

Table 2: Public Bond Issues, FY 1980-FY 1987

(in billions of yen, revised general account budget)

| FY | Bond Issues* | Dependence** | Outstanding Debt | Percent of GNP |
|---|---|---|---|---|
| 1980 | Y14,270 | 32.7% | Y70,509.8 | 28.8% |
| 1981 | 12,900 | 27.6 | 82,273.4 | 31.7 |
| 1982 | 14,345 | 30.2 | 86,482.2 | 35.4 |
| 1983 | 13,790 | 27.1 | 109,694.7 | 38.6 |
| 1984 | 12,865 | 25.0 | 121,693.6 | 40.1 |
| 1985 | 12,438 | 23.4 | 134,431.4 | 41.9 |
| 1986 | 11,495 | 21.4 | 145,400.0 | 43.4 |
| 1987 | 11,861 | 21.1 | n.a. | n.a. |

*Includes both construction and deficit-financing bonds.
**As percent of total revenues.

Source: Ministry of Finance

The supplementary budget provides Y1.36 trillion ($9.7 billion) in additional public works spending and Y179 billion ($1.3 billion) in subsidies for public housing. Extra funds are also earmarked for foreign aid, including $100 million in untied loans for African countries. Moreover, Tokyo plans to purchase an additional $1 billion worth of foreign products, including two long-range passenger planes, two supercomputers, five rescue planes and 13 helicopters. This will sharply increase government purchases of foreign goods, which totaled Y39.4 billion ($281 million) in the October 1985-September 1986 period.

Japanese officials believe the economic stimulus package will enable the economy to reach the government's outlook of 3.5 percent real growth in FY 1987. Private analysts, however, are generally less optimistic. Sumitomo Bank, for example, thinks that the package will boost growth 1.1 percentage points to 2.9 percent and doubt that its effect on the trade imbalance will be as great as many expect. Another recent report by the Bank of Japan estimates that a Y3 trillion ($21.4 billion) increase in government spending will reduce the country's trade surplus by $1.5 billion over two years, while cutting the U.S. trade deficit by less than $1 billion.

Randall S. Jones

## Kuranari Pledges New Aid Package For ASEAN Nations

During a three-day mid-June visit to Singapore to attend the conference of foreign ministers of the Association of Southeast Asian Nations, Foreign Minister Tadashi Kuranari promised ASEAN a new aid package. In honor of the organization's twentieth anniversary and in response to growing demands by the groups members, Tokyo will offer an assistance fund "of substantial proportions" at the group's summit meeting in Manila this December.

Few of the specifics have been divulged yet, mainly because Japanese officials want to respond to ASEAN requests. Before the December meeting Tokyo

study the issue. This approach, it hopes, will give the proposal a better chance of passage when the group meets next year. The United States, however, remains opposed to all forms of whaling and is in possession of considerable leverage because it controls access to this country's rich coastal fishing grounds.

Tatsuo Saito, the Japanese IWC commissioner, said he was "disappointed at the decisions taken" at the meeting. Charging that "there is a constant vote against Japan, even by members who have never attended" the scientific committee meetings, Mr. Saito resigned from the IWC after the stinging votes. It is not clear if Tokyo will appoint another representative; to date there has been no formal reaction from the United States. Japan's official withdrawal from the commission could set off wide aftershocks, especially if Tokyo allows its fishermen to begin unrestricted whaling. Although this is unlikely, Mr. Saito's resignation does not improve the atmosphere for either the salmon fishing case or industry-wide fishing negotiations.

Jon Choy

Japan's Foreign Direct Investment Takes Off

Japanese foreign direct investment has been on an exponential growth track since March 1975, doubling every four years, most recently from $53.1 billion in March 1983 to $106 billion this past March. Staying on course will obviously be harder from here on, but if FY 1986 trends are any indication, overseas equity holdings should double again by March 1991. Japanese businesses invested a record-shattering $22.3 billion abroad in the April 1986-March 1987 period after adding $12.2 billion to their foreign direct investment position in FY 1985 and $10.2 billion in the previous fiscal year. The 23.2 percent appreciation of the yen against the dollar over the course of FY 1986 certainly made it less expensive for Japanese companies to put money into offshore business activities, but almost every other factor corporate planners weigh in considering foreign investment also signaled go.

However weak, the ongoing U.S. economic expansion and market conditions in other areas of the world exerted an enormous pull on Japanese manufacturers hobbled by the yen-triggered erosion of export competitiveness. At the same time protectionism in the United States and Europe, whether threatened or real, and the need for lower cost sources of supply gave export-oriented companies an extra incentive to invest in overseas production facilities. For service firms hemmed in at home by sluggish growth and limited opportunities for diversification, eased foreign investment regulations and the higher returns available abroad in such areas as real estate worked hand-in-hand to swell the outflow of direct investment funds.

The United States remained the prime location for Japanese foreign direct investment in FY 1986, attracting a whopping $10.2 billion. While this figure was nearly twice FY 1985's then-record tally, Japanese companies again earmarked about one-fifth of their outlays -- or approximately $2.1 billion -- for the construction or acquisition of U.S. production and assembly facilities. Roughly $1 billion of this money went into plants to make industrial and consumer electronics products and nonelectric machinery, with most of the rest spread almost equally among automotive equipment, chemicals and metals.

Table 1: Japan's Foreign Direct Investment by Country, FY 1982-FY 1986

(in millions of dollars)

| | FY 1982 | FY 1983 | FY 1984 | FY 1985 | FY 1986 | Cumulative March 31, 1987 |
|---|---|---|---|---|---|---|
| United States | $2,738 | $2,565 | $3,360 | $5,395 | $10,165 | $35,455 |
| Canada | 167 | 136 | 184 | 100 | 276 | 1,951 |
| North America | 2,905 | 2,701 | 3,544 | 5,495 | 10,441 | 37,406 |
| Panama | 722 | 1,223 | 1,671 | 1,533 | 2,401 | 8,841 |
| Brazil | 322 | 410 | 318 | 314 | 270 | 4,857 |
| Mexico | 143 | 121 | 56 | 101 | 226 | 1,556 |
| Caymans | 6 | 1 | 1 | 132 | 930 | 1,279 |
| Bahamas | --- | 1 | 97 | 298 | 792 | 1,247 |
| Peru | 185 | --- | 6 | 10 | --- | 696 |
| Bermuda | 5 | 14 | 29 | 148 | 16 | 617 |
| Latin America | 1,503 | 1,878 | 2,290 | 2,616 | 4,737 | 20,373 |
| Indonesia | 410 | 374 | 374 | 408 | 250 | 8,673 |
| Hong Kong | 400 | 563 | 412 | 131 | 502 | 3,433 |
| Singapore | 180 | 322 | 225 | 339 | 302 | 2,571 |
| Korea | 103 | 129 | 107 | 134 | 436 | 2,118 |
| Malaysia | 83 | 140 | 142 | 79 | 158 | 1,283 |
| Taiwan | 55 | 103 | 65 | 114 | 291 | 1,051 |
| Philippines | 34 | 65 | 46 | 61 | 21 | 913 |
| Thailand | 94 | 72 | 119 | 48 | 124 | 884 |
| China | --- | --- | 114 | 100 | 226 | 513 |
| Asia | 1,384 | 1,847 | 1,628 | 1,435 | 2,327 | 21,790 |
| Kuwait | 41 | 66 | 55 | 34 | 41 | 1,309 |
| Iran | 0 | 1 | 0 | 0 | --- | 1,003 |
| Middle East | 124 | 175 | 273 | 45 | 44 | 3,016 |
| United Kingdom | 176 | 153 | 318 | 375 | 984 | 4,125 |
| Netherlands | 73 | 113 | 452 | 613 | 651 | 2,337 |
| Luxembourg | 127 | 265 | 315 | 300 | 1,092 | 2,308 |
| West Germany | 194 | 117 | 245 | 172 | 210 | 1,552 |
| France | 102 | 93 | 117 | 67 | 152 | 970 |
| Belgium | 64 | 126 | 71 | 84 | 50 | 793 |
| Switzerland | 79 | 37 | 229 | 60 | 91 | 753 |
| Spain | 19 | 52 | 140 | 91 | 86 | 601 |
| Europe | 876 | 990 | 1,937 | 1,930 | 3,469 | 14,471 |
| Liberia | 434 | 323 | 281 | 159 | 289 | 2,744 |
| Africa | 489 | 364 | 326 | 172 | 309 | 3,678 |
| Australia | 370 | 166 | 105 | 468 | 881 | 4,502 |
| Oceania | 421 | 191 | 157 | 525 | 992 | 5,234 |
| Total | 7,703 | 8,145 | 10,155 | 12,217 | 22,320 | 105,970 |

Source: Ministry of Finance

Table 2: Japan's Foreign Direct Investment by Sector, FY 1982-FY 1986

(in millions of dollars)

| | FY 1982 | FY 1983 | FY 1984 | FY 1985 | FY 1986 | Cumulative March 31, 1987 |
|---|---|---|---|---|---|---|
| Manufacturing Sector | $2,076 | $2,588 | $2,505 | $2,352 | $3,806 | $28,206 |
| Food Products | 78 | 77 | 118 | 90 | 127 | 1,218 |
| Textiles | 67 | 174 | 85 | 28 | 63 | 2,146 |
| Wood Products | 76 | 91 | 115 | 15 | 57 | 1,178 |
| Chemicals | 322 | 450 | 223 | 133 | 355 | 4,337 |
| Metals | 468 | 479 | 718 | 385 | 328 | 5,518 |
| Nonelectric Machinery | 164 | 169 | 185 | 352 | 626 | 2,597 |
| Electric Machinery | 267 | 502 | 409 | 513 | 987 | 4,734 |
| Transport Equipment | 439 | 486 | 437 | 627 | 828 | 4,201 |
| Other | 195 | 160 | 215 | 208 | 435 | 2,276 |
| Nonmanufacturing Sector | 5,478 | 5,357 | 7,429 | 9,536 | 17,949 | 74,285 |
| Agriculture/ Forestry | 40 | 18 | 26 | 12 | 15 | 795 |
| Fisheries | 22 | 17 | 24 | 42 | 52 | 494 |
| Mining | 685 | 382 | 484 | 598 | 669 | 12,424 |
| Construction | 44 | 55 | 112 | 94 | 250 | 1,047 |
| Trade/Sales | 1,899 | 1,164 | 1,482 | 1,550 | 1,861 | 14,538 |
| Banking/Finance/ Insurance | 533 | 1,167 | 2,085 | 3,805 | 7,240 | 18,099 |
| Services | 702 | 622 | 681 | 665 | 1,560 | 6,246 |
| Transportation | 924 | 1,363 | 1,651 | 1,240 | 1,925 | 7,826 |
| Real Estate | 354 | 375 | 430 | 1,207 | 3,997 | 6,531 |
| Other | 276 | 193 | 454 | 322 | 379 | 6,285 |
| Branch Offices | 149 | 200 | 221 | 329 | 566 | 2,884 |
| Real Estate Transactions* | --- | --- | --- | --- | --- | 595 |
| Total | 7,703 | 8,145 | 10,155 | 12,217 | 22,320 | 105,970 |

*Overseas real estate transactions have been excluded from Japan's foreign direct investment data since December 1, 1980 because of changes in the Foreign Exchange and Foreign Trade Control Law.

Source: Ministry of Finance

Japanese corporations also continued to expand their presence in the American banking, finance and insurance sector, investing an estimated $2 billion. Another $1 billion or so was channeled into the U.S. sales organizations of Japanese companies. What set FY 1986 apart from earlier periods, though, was that Japanese investors put more money into American real estate -- some $3.6 billion worth -- than in any other sector of this country's economy.

In adding $3.5 billion to their equity holdings in Europe during the 12 months through March 1987, Japanese businesses also came close to doubling their FY 1985 investments in this area of the world. Financial institutions remained the major players, putting another $2.3 billion into banking, finance and insurance subsidiaries and affiliates. More money was invested in European production facilities, but the $0.4 billion addition paled in comparison with the amount going into the U.S. manufacturing sector. Europe and the United States were on a more equal footing in terms of the expansion of commercial enterprises since Japanese distributors invested $0.4 billion in European sales organizations.

While Japanese foreign direct investment in FY 1986 continued to be skewed toward the United States, Europe and other industrial countries, a bigger volume of capital did flow into the economies of Latin America and Asia. At $4.7 billion, in fact, Japanese investment in Latin America was almost twice as large as FY 1985's total. The transportation industry remained a magnet, attracting $1.5 billion-plus, mainly to Panama, but this time around the financial industry was the main draw as businesses in Japan invested $2.5 billion in such tax havens as the Caymans, the Bahamas and Panama. Japanese corporations continued to pursue a more diversified investment strategy in Asia. One-third of the $2.3 billion invested in this region during the April 1986-March 1987 period went into production facilities, particularly for electronics, with the rest divided among the services, financial, mining and commercial sectors.

The huge flow of funds going into the United States during FY 1986 reinforced North America's position as the top location for Japanese foreign direct investment. As of March 1987 businesses had a $37.4 billion equity stake in this country and Canada. The biggest block of money -- $9.9 billion -- was in the manufacturing sector, with about one-fourth of this total in electronics companies. The commercial sector, the top draw until FY 1985, ran a distant second at $8.5 billion. Moreover, it could slip another notch or two in the rankings this year if FY 1986's investment pattern is repeated since banks and other financial institutions already had $6.3 billion invested in North America at the end of March 1987 while Japanese real estate holdings were valued at $5.8 billion.

Asia, the leading offshore investment site for Japanese corporations through March 1983, managed to retain the number-two spot with a $21.8 billion total at the end of FY 1986, but its hold was tenuous since investors had equity interests of $20.4 billion in Latin America. Of the amount invested in Asia, $8.3 billion was in metals, chemicals, textiles, electronics and other manufacturing operations and $6.4 billion was in mining. In Latin America, though, transportation services were the top investment sector with a March 1987 total of $6.1 billion, followed by manufacturing ($4.8 billion) and banking ($4.3 billion).

With a record $3.8 billion going into overseas production facilities during FY 1986, manufacturing continued to represent the leading edge of Japanese foreign direct investment activity. By March 1987 Japanese corporations had channeled $28.2 billion into production facilities abroad, including $9.9 billion in North America and $8.3 billion in Asia. Thanks to FY 1986's unprecedented $7.2 billion addition, the financial sector moved up two positions in the rankings to the number-two position with a cumulative total of $18.1 billion. This amount was divided roughly in thirds among North America ($6.3 billion), Europe ($6 billion) and the rest of the world anchored by Latin America ($4.3 billion). The third-largest concentration of Japanese equity funds was in overseas sales operations, where businesses had a March 1987 stake of $14.5 billion, three-fifths of which was in the United States and Canada. Holding down fourth place was mining, with the $12.4 billion total as of last March split almost evenly between Asian countries, mainly Indonesia, and the rest of the world.

Susan MacKnight

Notes

Senate Trade Bill - True to his word, Senate Majority Leader Robert Byrd (D, W.Va.) extended floor consideration of the trade bill (S 1420) during the week of June 22 to a Saturday session. Having said that the bill should be completed before the July 4 recess, Sen. Byrd had to concede that this would not be possible -- especially after three days of floor debate produced few results. Most of the debate focused on political issues rather than the trade-specific amendments that most observers believe will be the meat of the debate. Even the Saturday session became a lengthy debate on the question of a balanced budget amendment rather than trade law.

Still, there was some movement. Most significant was an unsuccessful attempt by Sen. Arlen Specter (R, Pa.) to allow firms to sue for dumping damages in the courts. The amendment failed by a vote of 69-27; some observers had been concerned that passage of this proposal would set a dangerous (and protectionist) precedent. Much of the substantive work, however, is expected to be done during the week of June 29 and immediately following the July 4 recess.

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The views expressed in this report are those of the authors and do not necessarily represent those of the Japan Economic Institute.